No. 21069

In the

United States Court of Appeals

For the Ninth Circuit

In the matter of
LEGEND CITY, INC.,
Debtor.

PHILLIP NEAL ADAMS, et al,
Appellants,

v.

WALTER E. FULFORD, TRUSTEE,
Appellee.

BRIEF OF APPELLANTS

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JURISDICTION

This matter arises from proceedings for corporate reorganization under Chapter X of the Bankruptcy Act, 11 U.S.C. Secs. 501-676. The petition of the debtor Legend City, Inc. was filed January 7, 1965 (R.1).[1] It was approved and a trustee was appointed January 11, 1965 (R.14) who duly filed his bond, qualified for

[1]The record in this case consists of a volume of court filings plus the transcripts of various hearings. The court filings have been numbered consecutively from the first page through the last so that, *e.g.*, an item on p. 400 will be cited "R.400."

the office and entered into his duties. The petition was at all times resisted by the secured creditors of the debtor, who bring this appeal here.[2]

On March 14, 1966, the trustee petitioned the court for issuance of trustee's Certificates of Indebtedness No. 3 in the amount of $100,000 for the purpose of operating the debtor's business during 1966 and 1967 (R.538). The petition stated that if the certificates were not authorized, the debtor would have to be adjudicated a bankrupt or the Chapter X proceedings would have to be dismissed (R.538). The appellants filed a responsive pleading (R.559) and a memorandum (R.567) urging the court to adjudicate the debtor a bankrupt or to dismiss the Chapter X proceedings. On March 29, 1966, appellants moved the court for an order of sequestration of rents and profits from operation of the debtor's business (R.585). A hearing was held on these matters March 23, 24, 29, 30 and 31, 1966 (T. III),[3] and on April 14, 1966, the court granted the trustee's petition and denied appellants the relief they sought (R.640, 660). This appeal from the order granting the trustee's petition (R.640)[4] and from the order denying appellants' motion for sequestration (R.660)[5] was taken April 18, 1966, appropriate bond being filed the same day (R.661, 663).

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[2]These are Phillip Neal Adams and Charlotte Adams, his wife; L. Grant Robinson and Ethna C. Robinson, his wife; C. Birk Lefler and Peggy Kelso Lefler, his wife; and J. Talmadge Jones and Vera Jean Jones, his wife.

[3] The record contains three transcripts of hearings. The transcript of proceedings of February 1 and February 15, 1965 will hereinafter be designated as T.I; the transcript of proceedings of March 5 and March 19, 1965 (two volumes) will hereinafter be designated as T. II; and the transcript of proceedings of March 23, 24, 29, 30 and 31, 1966 (three volumes) will hereinafter be designated as T. III.

[4]The court's orders were dated April 14, 1966, but appellants were not informed of the existence of them until April 15, and the notice of appeal filed by appellants is therefore erroneous by one day as to the date of the orders appealed from.

[5]See n. 4 *supra.*

The court below had jurisdiction to hear the appellants under 11 U.S.C. Sec. 606 and this Court has jurisdiction under 11 U.S.C. Secs. 521 and 47.

STATEMENT OF FACTS

A. Pre-litigation History.

The debtor, Legend City, Inc., an Arizona corporation, with approximately 10,300 shareholders (T. III 39), owned and operated an amusement park in the City of Tempe, Maricopa County, Arizona. The 58 acres on which the park is located contain numerous buildings which house merchandising and display facilities including restaurants, gift shops, theatres and other general merchandise stores, as well as a number of entertainment attractions and rides (R.1).

Operations of the park began on June 29, 1963 (R.116) and were suspended on October 31, 1964 (T. II 32). Appellants, the principal creditors of the debtor, were owed $640,135.36 on the date of suspension (R.1). This debt was secured by a mortgage on substantially all of the real and personal property of the debtor. The mortgage included an assignment of all rents and profits and an assignment of whatever interest the debtor might have in the leases and licenses granted to persons operating within the park as concessionaires. This mortgage was dated March 16, 1964, and on its face bears seven per cent interest per annum, to be raised to eight per cent interest after a default (Exhibit I).[6]

Obligations to other secured creditors include the following:

1. $15,000 on a note and mortgage dated March 17, 1964 (R.1).

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[6]There were a number of exhibits introduced in evidence at the March, 1966 hearings which are part of the record on appeal. These will be identified by the exhibit number or letter affixed to it at the hearing in the District Court. See Appendix A to this brief for a full list of the exhibits.

2. Promissory note and mortgage for $55,000 dated November 11, 1964 (R.1).[7]

3. A purchase money chattel mortgage with an unpaid balance of $30,000 (T. II 137, T. III 181).

B. State Court Receivership.

As a result of defaults in the fall of 1964, appellants instituted a judicial foreclosure action in the Maricopa County, Arizona, state court, Cause No. 168904. After an adversary hearing, including the taking of testimony, the state court found that the following defaults had occurred:

> ". . . . The defendant Legend City, Inc. has failed to pay the real property taxes due for the first half of 1964 on the real property involved in this action, such real property taxes now being delinquent, that the defendant Legend City, Inc. has failed to pay the premiums for fire insurance and liability insurance covering the property involved in this action, such policies having lapsed prior to the filing of this action, that the defendant Legend City, Inc. has failed to pay Federal withholding taxes and that the Internal Revenue Service has filed of record its lien in connection with such taxes, that the defendant Legend City, Inc. has been financially unable to maintain any security force or other method of protecting and preserving the property involved in this action and has temporarily ceased operation of the business known as Legend City . . ." Order Appointing Receiver, Civil Cause No. 168904, December 11, 1964.

The trial court found Legend City to be insolvent and appointed a receiver. A state receiver duly took possession until he surrendered it to the federal receiver in these proceedings (R.76). The state court receiver has filed a report and account but has not been discharged.

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[7]This note and mortgage were executed less than four months before the Chapter X proceedings for an antecedent debt and may be a voidable preference as to the security interest.

C. Chapter X Proceedings.

1. Preliminary and 144 proceedings, and evidence thereon; role of the SEC.

While the state court foreclosure was under way, the debtor on January 7, 1965, filed a voluntary petition for reorganization under Chapter X, Sec. 128 of the Bankruptcy Act, 11 U.S.C. Sec. 528. The trial court ex parte approved the petition and appointed Walter E. Fulford as trustee on January 11, 1965 (R.14). This order is referred to hereinafter as the Chapter X Court's initial order of approval. That order specifically stayed the pending mortgage foreclosure action and, among other things, authorized the trustee to operate and manage the amusement paark owned by the debtor.

Appellants on January 19, 1965 moved for an order to modify the court's initial order of approval, for an order vacating the stay of the mortgage foreclosure proceedings and for an order dismissing the Chapter X proceedings (R.27, 41). The debtor's petition had alleged that any plan of reorganization would have to modify the rights of secured creditors. By virtue of Sec. 179 of the Act, 11 U.S.C. Sec. 579, the consent of appellants as holders of more than two-thirds of the total secured indebtedness would be required for any plan. In their motion to modify, appellants alleged that they would not then or thereafter consent to any plan of reorganization which modified or altered their rights in any way. Appellants therefore asserted that the petition was not filed in good faith as defined in Sec. 146(3), 11 U.S.C. Sec. 546(3), since there was no reasonable possibility of a reorganization plan ever being effected.

The first hearing in this matter was on appellants' motions on February 1, 1965, and at that time appearances were made by appellants as secured creditors, the debtor corporation, the trustee, other secured creditors and the Securities and Exchange Commission. The Commission appeared by authority of Secs. 161 and 208, 11 U.S.C. Sec. 561 and 608. They supported the continued

operation of the park by the trustee in this and in all subsequent hearings (T. I 27-33, T. II 80-85, 250-52, T. III 469-72).

At this initial hearing, no new factual information was presented to the court concerning the financial situation of the debtor beyond the material contained in the pleadings. On February 1, 1965, the district court denied all motions of appellants (R.84).

Following the denial of appellants' motion, the trustee petitioned the court for an order authorizing him to issue a certificate of indebtedness to the extent of $10,000 (R.90). This application was for the purpose of maintaining the amusement park until the plan of reorganization was filed, which under the court's initial order of approval was due by April 5, 1965. The appellants opposed the issuance of such certificate of indebtedness.

The hearing on the application for this certificate was the first actual review by the court of values. The amount of stock which had been sold in this enterprise was something over $3,200,000.[8] The value which the petition alleged for the land and personalty owned by the debtor was $3,762,286.49 (R.1), taken directly from the debtor's books of account. However, the actual testimony at the first certificate hearing by the court's trustee was that the value of the real property was approximately $900,000 and that the salvage value of personal property was $250,000 to $300,000, making a total value for the assets of the corporation of $1,150,000 to $1,200,000 (T. I 163-64). A professional real estate appraiser, qualified as an M.A.I., Mr. John T. Hansen, testifying for appellants, set the land value only at a maximum of approximately $450,000 (T. I 79). Thus, given the most optimistic statement of values as shown on the record, the assets at best had a value of approximately $1,200,000, to be contrasted with then admitted obligations to creditors of over $1,000,000. If one modifies this to take into consideration the

[8]The exact figure as shown in the December 31, 1964 balance sheet (which was filed August 16, 1965) was $3,292,796.07; see Exhibit A, which is appendix D to this brief.

view of the only qualified appraiser who testified, the values were about $750,000 as against obligations of $1,000,000.

Nonetheless, the district court entered an order authorizing the issuance of the certificate of indebtedness on February 16, 1965 (R.100). The order provided that the certificate should be paid out of the debtor's funds by August 16, 1965. It has in fact never been repaid, and the holder of the certificate, The Pioneer Bank of Arizona, has filed a petition with the district court to compel its payment (R.524). The court has never granted permission to the trustee to extend or exceed the due date of the certificate so the certificate is, in fact, in default and has been in default since August 16, 1965.

The court's initial order of approval provided that the trustee was to prepare and file a plan of reorganization or a report of his reasons why a plan could not be effected on or before April 5, 1965, and that a hearing on such plan or report or a hearing pursuant to Sec. 236(2), 11 U.S.C. Sec. 636(2), would be held on May 7, 1965 (R.14). In addition, the trustee was to prepare a statement of his investigation of the property, liabilities and financial condition of the debtor, the operation of its business and the desirability of the continuance thereof on or before March 12, 1965 pursuant to Sec. 167(5), 11 U.S.C. Sec. 567(5).[9]

Despite this order, the trustee has not to this day filed a plan of reorganization nor has he filed any of the reports required under Sec. 167, 11 U.S.C. Sec. 567, on the debtor's financial status. No full report of the conduct, property, liabilities and financial condition of the debtor or report on the desirability of continuance of the business has ever been filed with the court during the year and one half the Chapter X proceedings has been pending.

As has been noted, the trustee originally sold a $10,000 cer-

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[9]A first extension on these requirements was given by the court ex parte (R.107), and thereafter a continuance was granted, which to date has amounted to an indefinite stay, on March 24, 1965 (R.137).

tificate of indebtedness. On March 22, 1965, he sought a second certificate of indebtedness of $50,000 (R.112), the purpose of which was to finance park operations in the summer of 1965. The new amount was to be repaid out of operating income that summer. This certificate was authorized on March 25, 1965 (R.139), but has not in fact been paid and has been in arrears since September 21, 1965.

The 144 hearing was held between March 5 and March 19, 1965. The issue in the 144 hearing was whether the original petition had been filed in good faith in view of the fact that, as developed above, there was no possibility of reorganization. The court ruled against appellants on the 144 hearing (R.168) and, there being no appeal from that order,[10] the proceedings are of no further consequence except for one item of fact. The testimony at this hearing was that the net operating loss of the debtor during 1964 was $85,000 (T. II 37). Later financial statements filed by the trustee show the true loss to have been $138,795.33 for the last elevent months of 1964. Exhibit A, Appendix D to this brief.

2. Court proceedings between the 144 hearing and Certificate No. 3.

The 144 proceeding was concluded in March of 1965. The application for Certificate No. 3 was made in March of 1966. During this twelve-month period, the following legal proceedings occurred:

(a) The most significant legal proceedings during this one year period is in fact a negative—there were no legal proceedings concerning a plan of reorganization and appellants contend that there should have been. As noted above, by virtue of the court's order of March 24, 1965, giving the trustee an indefinite time in which to file a reorganization plan, there never was a

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[10]An appeal was taken but was later dismissed in accordance with a stipulation which will be described later.

reorganization plan filed and there has never been a hearing concerning any such plan.

(b) On April 13, 1965, the trustee filed a petition for permission and authority to reject certain executory contracts of the debtor pursuant to Sec. 116(1), 11 U.S.C. Sec. 516(1), of the Act which allows the court to "permit the rejection of executory contracts of the debtor . . ." (R.174, 185). This involved concessionaire contracts in which appellants had a security interest. The appellants resisted the petition on the grounds that the contracts sought to be rejected were not, in fact, executory, but represented leasehold interests or estates not within the contemplation of Sec. 116(1). Following hearing and extended negotiations, a written stipulation was entered into by the Chapter X trustee, the concessionaires involved, the appellant-mortgage holders and, to a limited extent, the debtor corporation (R.299). This stipulation was followed by a master's report made pursuant to the stipulation, which allowed the trustee and the experienced park operator with whom the trustee had an operating contract approved by the court (R.145) to operate the park until November 1, 1965, under interim revised agreements with the concessionaires. Under the stipulation and the report and the order which followed, all parties were to be free to reassert their rights and position at any time after November 1, 1965 (R.299, 375).

(c) On November 12, 1965, appellants moved the court for an order modifying the stay to permit resumption of their pending state court mortgage foreclosure action (R.450). A stipulation was entered into and an order issued allowing the foreclosure to proceed under certain limited conditions and based on a certain time schedule (R.502). The order, dated December 13, 1965, gave the trustee the option to have the amount and validity of appellants' claim determined in U. S. District Court rather than in state court, if he exercised that privilege prior to June 1, 1966. It also prohibited appellants from having final judgment entered by the state court in the mortgage foreclosure proceedings and

prohibited them from having any judicial foreclosure sale, without prior consent of the district court.

(d) Meanwhile, neither of the earlier trustee's certificates had been paid. On January 1, 1966, the Pioneer Bank of Arizona, which had purchased Certificate of Indebtedness No. 1, moved the court for an order directing payment of that certificate (R.524). The appellants objected to the granting of that motion on the grounds that Certificate of Indebtedness No. 1 had specifically been made prior only to the payment of other obligations of the estate save and except for real and personal property taxes, and that by December 31, 1965, almost $40,000 in real property taxes assessed against the debtor were due and delinquent. The hearing on this petition had been repeatedly postponed at the request of the trustee.[11]

3. Operating expenses and financial situation, March 1965-March 1966; the financial situation at the time of the instant proceedings.

As noted above, as of March 1965, on the basis of the record in these proceedings, the assets of Legend City were either approximately $200,000 more than the liabilities or approximately $250,000 less than the liabilities, depending upon which view was to be followed. During this year the trustee, who had stated that a feasible plan of reorganization could be formulated by April 5, 1965 (R.74), entered into a court-approved contract with an experienced amusement park operator, Mr. T. H. Browning of T. H. Browning & Associates, Detroit. The trustee had felt that the deficiency of the park was not in attendance but in management and that with proper management the park could service its indebtedness and show a profit (R.152). He forecast for the operating season 1965 an estimated income of $731,468 and an estimated expense of $473,666 (R.162-63). In fact, the event belied this optimism. The trustee's December 31, 1965 balance

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[11]Under the laws of the State of Arizona, unpaid property taxes are prior in right to even the first mortgage lien of appellants. *Ariz. Rev. Stat. Ann.* Sec. 42-312 (1956).

sheet shows operating income of $652,642.93 and total operating expense of $697,040.85.[12] Given these figures, there was a loss of $44,397.92. However, these are operating costs only. If an adjustment is made for debtor incurred depreciation and interest, those taxes which were paid, and those administrative expenses of the trustee which were paid, the total expenses were $858,980.83, for a 1965 calendar year loss of $206,337.90.[13]

On March 14, 1966, the trustee petitioned for issuance of still another trustee's certificate of indebtedness, this one to be in the amount of up to $100,000 (R.538). This is the instant proceedings from which appeal has been taken and details concerning it are set forth in the next section. However, using the period of March-April, 1966, as a convenient date for summarizing valuation figures, the assets and liabilities of the enterprise as of that period are as follows:

(a) Values.

The trustee's estimate of value as of this period, including all assets and assuming as he did that the park can be sold as a going concern amusement park, is $1,650,000. This represents a land value of $900,000 (T. III 381) and a going concern value of $750,000 covering all buildings, rides and equipment (T. III 386). On the other hand, if it cannot be sold as a going concern, then the trustee's estimate of the salvage value of the equipment is $250,000 (T. III 386). The trustee gave no basis for his "going concern value" figure. It was not based on the prior operating history of losses of the debtor, although he did state that the park would be worth more than it is now worth if it were operating at a profit (T. III 149). It is also not based on any new services or plans by which the loss picture could be changed,

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[12]Figures are taken from Exhibit 5, the income and expense portion of which is attached as Appendix B to this brief.

[13]See the trustee's reconciliation of December 31, 1965, Exhibit 8, attached to this brief as Appendix C.

since no such devices or plans were presented at the 1966 hearings.[14]

These opinions of value include no evidence by an appraiser. On August 4, 1965, the court authorized the trustee to retain an appraiser to prepare an appraisal but no appraiser's report has even been submitted by the trustee (T. III 381). The appellants' evidence of value is reached by the $450,000 land value of its appraisal plus the trustee's $250,000 salvage value of equipment (T. III 384).

The value estimates therefore range from $700,000 (appellants'); $1,150,000 (trustee's land plus salvage); and $1,650,000 (trustee's land plus going concern valuation). In evaluating the figure which depends upon a sale of the enterprise as a going concern, the court may consider that there has been no firm purchase offer in the one and one half years of this proceedings.[15]

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[14]"Q (by Mr. McGarry) With reference to this going concern value that you told the Court about, Mr. Fulford, as I understand it, Mr. Kelly, your M.A.I., told you that with what you had available by way of facts and figures, he could not begin to give you a going concern value; is that about what he told you?

A (by Mr. Fulford) That is in substance. There was one other reason, too.

Q The expense of going to other parks and looking at other parks?

A That is correct.

Q Right. What criteria did you use in coming up with your $750,000 going concern value?

A On the improvements on the park?

Q Yes.

A Various conversations with people that last year came out to look at the park with the thought of having something to do with it.

Q How did —

A They are listed in the schedules. As a park, in relationship to what it costs if a corporation or an individual were to buy it, to operate it as a park, it is a real good value. If they don't want to operate it as a park, it is probably worth real estate and salvage." (T. III 388-89).

[15]Troy Browning, the experienced park operator who managed the park during the 1965 season for the trustee, told the court prior to the 1965 season that he would pay $1,500,000 for it on his terms, which

(Continued on Page 14)

(b) Debt.

The trustee's estimate of total debt is $1,244,569.96.[16] However, this figure does not include liabilities or expenses for administration of this proceedings which according to the trustee may well amount to $125,000 (T. III 378); it does not include any adjustment for the increase of interest on the appellants' mortgage from seven to eight per cent to which it became entitled two years ago when the mortgage went into default (T. III 376); it includes nothing for attorneys' fees for the foreclosing for appellants, which might be a substantial sum indeed (T. III 379-80); it does not include added charges on the other mortgages, the 1966 property taxes or the up to $100,000 of Certificates No. 3 which the court has now authorized.

In short, the existing debts of this enterprise, based on the trustee's own figures, are now equal to or more than the total value of the property,[17] taking the trustee's most optimistic estimate of that value. *If the trustee's most conservative estimate of value is followed, the debts now exceed all assets by approximately half a million dollars; and if the appellants' figures are followed, the debts exceed all assets by about $850,000.*

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called for very easy financing (T. II 67, 73-74). The offer was not repeated after the 1965 disaster. Robert Rice, a man who has been in the amusement park business many years and who was manager of Legend City during part of the pre-Chapter X period, estimated the value of the entire park at $1,000,000, but did not offer to buy it (T. II 184).

[16]Trustee's balance sheet of December 31, 1965, Exhibit 8, Appendix E hereto.

[17]It is significant to note that, despite the money poured into Legend City by the trustee and his operator, Browning, during 1965, the value of the assets has not increased since December 31, 1964 (T. III 390-94). For comparison purposes, the balance sheet of Legend City on December 31, 1964, which is exhibit A, is attached to this brief as Appendix D. It, of course, reflects only book values of the assets, but the liabilities are all real. The balance sheet of December 31, 1965 (the latest available for the March hearings), which is Exhibit 8, is attached to this brief as Appendix E.

D. The Instant Proceedings.

As noted, in March of 1966, the trustee petitioned for issuance of a third certificate of indebtedness, this one to be $100,000. The park having lost $206,337.90 in the 1965 calendar year, the trustee now proposed to operate it for two additional years. He did not propose to pay any interest or any portion of the mortgage debt or property taxes with these funds or with the 1966 operating funds.

The trustee's petition for the certificate alleged that if this certificate were not authorized, the debtor would have to be adjudicated a bankrupt or the Chapter X proceedings would necessarily be dismissed (R.538). As is summarized in the Jurisdiction statement in the beginning of this brief, the appellants asked the court to adjudicate the debtor a bankrupt or to terminate the Chapter X proceedings and resisted altogether the issuance of the third certificate. Appellants' position was that whether the original orders had been right or wrong, the operating history of 1965 and the value testimony now available proved that Legend City is a hopeless endeavor. Appellants also moved for an order of sequestration of rents and profits from the operation of the business (R.585).

The hearing was held in late March, 1966 (T. III). The SEC supported the application for the certificate. It advocated that the question of whether the certificate should be given a priority over the secured debt of appellants should be reserved by the court to a later time (R.614). The court granted the trustee's petition and adopted the SEC's position concerning the postponement of determination as to what the priority of the $100,000 third certificate should be. It ruled against appellants on all points.

This appeal followed.

SPECIFICATION OF ERRORS

1. The district court erred in not requiring the adjudication of the debtor a bankrupt, or in not requiring the dismissal of Chapter X proceedings, either on its own motion or in response to

appellants' pleadings, in view of the operating history and present financial circumstances of the debtor corporation as presented at the hearing on issuance of trustee's certificates.

2. The district court erred in authorizing the issuance of Certificates of Indebtedness No. 3 in view of the facts presented to the court at the hearing concerning the issuance and in view of the operating history and present financial circumstances of the debtor corporation.

3. The district court erred in not fixing the priority of the Certificates of Indebtedness No. 3 as subsequent and junior to the lien of appellants' security interest, and erred in reserving jurisdiction to fix that priority at a later date, since it has no jurisdiction to do so.

4. The district court erred in not protecting appellants' security interest in property of the debtor by not granting appellants' motion for sequestration of rents and profits, particularly in light of the testimony as to the operating history and present financial circumstances of the debtor corporation brought out at the hearing on appellants' motion.

SUMMARY OF ARGUMENT

During the most recent hearings in this Chapter X proceeding, the hearings on the trustee's application for issuance of Certificate of Indebtedness No. 3, the district court should have adjudicated the debtor corporation a bankrupt under Section 236, 11 U.S.C. Sec. 636, and directed liquidation. This determination should have been made by the court on the basis of the factual data before it—the history of operating losses prior to the institution of the Chapter X proceedings, which included a loss of $138,795.33 during 1964 alone, an even greater loss in the trustee's operation of the park during 1965 of $206,337.00, and the fact that the trustee was granted every form of relief which he thought desirable for the successful operation of the park during 1965, and still lost more money than had been lost in the preceding year. Furthermore, the debts of the debtor are sub-

stantially as great as the most optimistic valuation of its assets, and the secured debts alone are greater than any realistic value of the debtor's assets. The court should have adjudicated the debtor corporation a bankrupt and ordered its liquidation because the trustee has not yet, in a year and a half, been able to file a report proposing a plan of reorganization or explaining why such a plan cannot be proposed, and because in fact the total record before the court conclusively proves that no plan can be proposed, adopted and put into effect. Since reorganization is the heart and purpose of the corporate reorganization provisions of the Bankruptcy Act, reorganization proceedings should and must be terminated when it becomes apparent that reorganization is impossible.

The same facts which show that the debtor corporation should be adjudicated a bankrupt are even more clear in indicating that the Certificates of Indebtedness No. 3 were improperly authorized and issued. A certificate of indebtedness in a corporate reorganization proceeding which will, or could have, priority over secured indebtedness should be issued only when the funds raised by the sale of the certificate will be used to put assets into the business so that secured creditors will not lose their security. The only time certificates of this type can be sold to be used for working capital, which might become dissipated, is when the value of the assets is clearly in excess of the value of the security of the secured creditors—a situation which is manifestly not true here. The accumulation of certificates of indebtedness and real property taxes ahead of appellants' security has in the past and will in the future impair and endanger appellants' security in violation of the rule of absolute priority for senior creditors.

The priority of Certificates of Indebtedness No. 3 was not fixed by the court's order. The court attempted to retain jurisdiction to fix priority at a later date. This not only renders appellants' security interests unmarketable, since there is no way to fix what appellants own until the priority of these certificates is established, but shows that the court was and is concerned about the fact that the property of the debtor corporation is not sufficient to

adequately secure appellants' mortgage indebtedness and the new certificates. Any jurisdiction the court may have had to issue the certificates at all was such that the court was required to place the certificates in a priority position junior in right to appellants' security interest and the court could not reserve jurisdiction to place it ahead of appellants' security interest if it later develops that there is insufficient property available to satisfy both appellants' claims and those of the certificate holders.

Under these circumstances, appellants had a right to have their motion for sequestration of rents and profits granted. In addition to their mortgage lien, appellants have a security interest in the rents and profits of the debtor corporation, and the issuance of the certificates of indebtedness No. 3 was for the purpose of allowing the trustee to operate the debtor's business. If any rents and profits should accrue in 1966 (a circumstance quite unlikely in view of the trustee's past record of operations), and if those rents and profits are not sequestered, appellants lose a valuable portion of the security for which they originally bargained.

The totality of the court's orders appealed from here are such that the appellants, who are the senior secured creditors of the debtor corporation and therefore should be placed in a position of priority to recover from the debtor's assets, have instead been required to finance an operation of the trustee which was ill advised in its inception and disastrous in its consequences. The totality of the rulings of the court appealed from here inequitably and illegally continues that situation.

ARGUMENT

I. The Debtor Corporation Should be Adjudicated a Bankrupt Under Section 236 of the Bankruptcy Act and be Liquidated Accordingly.

The debtor corporation is hopelessly insolvent and its situation is rapidly deteriorating. The trial court erred in not adjudicating it a bankrupt.

Let us strip the matter to bedrock: here is a corporation, which

at the most optimistic present valuation as shown in the record, is worth $1,650,000.00. Its hard liabilities, tangible, real and present, without any speculation at all, are substantially equal to this optimistic figure and are far higher than any realistic figure in the record. This unhappy enterprise is not merely flat broke, but it is continuing to go downward at the spectacular rate of the 1964 deficit of $138,795.33 and a 1965 deficit of a lusty $206,-337.90.

Nobody ever saw such a sick cat get well. The optimistic estimate assumes that someone might buy this enterprise, despite its deficits, at a good high price. But in a year and a half of waiting for the first serious or tangible offer, nothing has turned up; and there is no rational basis at all to suppose that a generous Midas awaits around the corner. As noted in the statement of facts, the trustee and his 1965 operator had carte blanche from the district court to make something out of this park if they could. The trustee was relieved of the necessity of abiding by "sweetheart contracts" with lessees and concessionaires. These concession contracts must be reinstated to their original form during the 1966 operating season and the trustee will not legally have the benefit of more favorable terms during 1966. Moreover, the trustee had his choice of experienced operators and chose the one he wanted to test his theory that new management would cure the deficiencies of the park. Furthermore, the trustee had a blank check—he drew two certificates of indebtedness, putting them ahead of common creditors, a privilege which no normal operator would have.

Despite the fact that the trustee and his operator were freed of the burdensome concession contracts, despite the fact that the trustee had an idyllic power over the situation which no normal businessman could expect, he still lost over $200,000 in the year 1965.

In summary, the trustee has taken a bad situation and turned it into a disaster. The book value of the assets, an item of doubt-

ful meaning in any event, has not increased noticeably in the year and a half since the trustee took over the park. The same assets have obviously depreciated in actual value during that period. The liabilities of the debtor, however, have been increased as a result of the trustee's 1965 operations, which resulted in a loss in excess of $200,000. The liabilities have been further increased by the unknown amount of administrative expense not reflected on the debtor's books, plus attorneys' fees which will have to be allowed secured creditors, extra interest caused by the delay in foreclosure, and other such expenses. At the early stages of the Chapter X proceedings, the appellants, as secured creditors, objected to the continuation in Chapter X on the ground that their security was in danger. Much evidence was presented to support their position. The net result of the court rejecting that argument and evidence has been to put these secured creditors in even greater jeopardy.

Significantly, there has never been a report by the trustee as to the results of his investigation of the property, liabilities, and financial condition of the debtor, whether the continuance of its business is desirable, or even if the debtor is solvent or insolvent as those terms are defined and used in Chapter X of the Bankruptcy Act. Apparently the trustee is planning to wait to make such a report to the court until at least one more full operating season has passed. Perhaps he is waiting for the 1967 season to pass as well. However, with the record that has been made, the court does not need the delivery of the Section 167, 11 U.S.C. Sec. 567, report to answer the question. The debtor corporation is hopelessly insolvent and there is no chance whatever that the trustee can reduce the insolvency to any significant degree, or propose a plan of reorganization that can keep the business alive.

The Chapter X court in this situation should terminate the proceedings and adjudicate the debtor a bankrupt. The district court should not grant further time for the proposal of a plan of reorganization if there is no immediate prospect that the debtor or the trustee can devise an acceptable plan, especially if a year

and a half has elapsed since filing the original Chapter X petition. See *John Hancock Mut. Life Ins. Co. v. Casey,* 141 F.2d 104 (1st Cir. 1944), *cert. denied,* 323 U.S. 713, 65 Sup. Ct. 39, 89 L. Ed. 574 (1944). The Court stated:

> ". . . . If the petition has been approved [under Section 144; 11 U.S.C. Sec. 544] and it later becomes evident to the judge that there is no reasonable prospect of effecting a plan of reorganization, it then becomes his duty to terminate the Chapter X proceedings, pursuant to § 236, ..." 141 F.2d at 107.

This is precisely the situation we have here. There simply is no possibility of the trustee or anyone else working out a practical and equitable plan of reorganization for this debtor. Not even the secured debts can be supported and eventually paid by the continued operation of the business, and under no event could there be anything at all for unsecured creditors and stockholders. This is so even without reference to the fact that the mortgage holder-appellants will not consent to any alteration or modification or change in their rights. In this matter, such consent would be necessary for any plan to be put into effect. Section 179 of the Bankruptcy Act, 11 U.S.C. Sec. 579; *Leas v. Courtney Co.,* 261 F.2d 13 (4th Cir. 1958); *Arey & Russell Lumber Co. v. American Nat'l Bank & Trust Co.,* 201 F.2d 508 (4th Cir. 1953). Not only is there no possibility of working out a practicable and equitable plan in this case, but also expenses are accumulating, the value of the debtor's assets is shrinking, and the total liabilities are increasing. All these factors justify the reorganization court adjudicating the debtor corporation a bankrupt, despite the fact that the debtor corporation and its stockholders still want reorganization. *Eddy Shipbuilding Corp. v. Bay Trust Co.,* 168 F.2d 993 (6th Cir. 1948).

In a situation such as this, a reorganization cannot possibly be feasible since it involves a greater debt than the property can support. *Wayne United Gas Co. v. Owens-Illinois Glass Co.,* 91 F.2d 827 (4th Cir. 1937):

> "However honest in its efforts the debtor may be, and however sincere its motives, the District Court is not bound to clog its docket with visionary or impractical schemes for resuscitation." 91 F.2d at 831.

Similar fact situations existed in *Oakland Hotel Co. v. Crocker First Nat'l Bank,* 85 F.2d 959 (9th Cir. 1936), and *In re Cosmopolitan Hotel, Inc.,* 85 F.2d 851 (10th Cir. 1936). In each of these proceedings, a hotel went into Chapter X and was operated by a receiver or a trustee at a loss during the pendency of the proceedings. The secured creditors would not consent to any plan which would jeopardize, eliminate or change their security interest and it did not appear that any angel would come forth with sufficient funds to purchase the secured creditors' interest. In each case, the dismissal of the petition under former Section 77B was held to be proper since no relief of the kind contemplated by Chapter X was possible. In this case the present posture of the Chapter X is such that adjudication and liquidation is clearly called for.

We appreciate that the Securities and Exchange Commission disagrees with us and has supported the position taken by the district court on this matter. While the Commission is respected, it is of course not sacrosanct. The Commission, in its role of an amicus adviser to the court, 6A *Collier, Bankruptcy,* ¶ 9.27 (14th ed. 1965) is supposed to advise the court from the broad point of view of the public interest and the general interest of investors. *Ibid.* Given these facts, this case must be regarded as a failure on the part of the Commission properly to advise. We think particularly unsound, and with an unsoundness which permeates its entire role in this matter, its recommendation concerning the sale of the third certificate of indebtedness without determining what the rights of the purchasers of that certificate would be. We shall develop that matter more precisely in its place, and pass it here only with the observation that the Commission has offered no specific facts to warrant the conclusions which it recommends.

The facts brought out in the various hearings on this matter

and the law as it is presented in this brief and as has been presented to the district court show that the debtor corporation should be declared a bankrupt, should be liquidated and, most important, should not be operated under a Chapter X trusteeship.

This is particularly true because the purpose of a reorganization proceeding is to reorganize, and there never has been and is not now any possibility of a successful reorganization plan being consummated.

Central to the purpose of Chapter X of the Bankruptcy Act is the necessity that a plan or reorganization be proposed and adopted. Section 146, 11 U.S.C. Sec. 546, provides that a petition filed under Chapter X may be dismissed even before a hearing if it is unreasonable to expect that a plan or reorganization can ultimately be effected. *Arey & Russell Lumber Co. v. American Nat'l Bank & Trust Co.,* 201 F.2d 508 (4th Cir. 1953). Section 167(6), 11 U.S.C. Sec. 567(6), requires the trustee to give notice to the creditors and stockholders so that they may, if they wish, submit suggestions for the formation of a plan within a time therein named. Section 169, 11 U.S.C. Sec. 569, provides that the judge *must* fix a time within which the trustee shall prepare and file a plan or a report of his reasons why a plan cannot be effected and must fix a time for a hearing on such a plan. Section 170, 11 U.S.C. Sec. 570, provides that other affected persons may also promulgate plans. If no plan is proposed or approved or if a confirmed plan is not consummated, the court must dispose of the proceedings under Section 236, 11 U.S.C. Sec. 636.

It is true that the district court has a certain amount of discretion and time leeway in determining whether or not a plan of reorganization can, in fact, be proposed, approved and ultimately consummated. Even the fact that a class of secured creditors announces in advance that it will not agree to a reorganization plan does not, in and of itself, make it impossible for a Chapter X reorganization petition to be filed in good faith, as

the term is used in Section 146, 11 U.S.C. Sec. 546. *York v. Florida So. Corp.,* 310 F.2d 109 (5th Cir. 1962), *cert. denied,* 372 U.S. 943, 83 Sup. Ct. 936, 9 L. Ed. 2d 968 (1963). This is the case even though it is necessary for creditors holding two-thirds of the claims filed and allowed by each class to approve the plan before it can be confirmed by the court. Section 179, 11 U.S.C. Sec. 579. A comparison of *York v. Florida So. Corp., supra,* with *Arey & Russell Lumber Co. v. American Nat'l Bank & Trust Co., supra, Leas v. Courtney Co.,* 261 F.2d 13 (4th Cir. 1958), and *Janaf Shopping Center, Inc. v. Chase Manhattan Bank,* 282 F.2d 211 (4th Cir. 1960), establishes a set of guide lines for the Reorganization Court in its initial determination whether or not a plan of reorganization is feasible.

If it is impossible for a plan of reorganization to be formulated and carried out without the consent of the secured creditors, and if the secured creditors announce in advance that they will oppose any plan of reorganization which modifies their rights in any particular, the petition is not filed in good faith because a plan of reorganization simply cannot be effected. *(Arey & Russell, Leas, Janaf.)* A typical situation where this might occur would be where a single secured creditor holds mortgages securing the entire debtor corporation's property, and where that property is worth less than the amount of the indebtedness to that creditor. However, if the property owned by the debtor corporation is worth substantially more than the secured indebtedness, it might be possible to formulate a plan in which the secured indebtedness could be entirely paid off and the business remain in operation. In such a case, the opposition of the secured creditor or creditors to the plan would not be determinative, at least in the initial stages. *(York)*

The initial petition in this case, however, shows that the situation presented to the court below was not within the guide lines of *York v. Florida So. Corp., supra.* The petition stated:

> "The rights of secured creditors must be altered or modified by the issuance of other securities and the cancellation or

> modification of their liens or otherwise. All such secured creditors will not consent to an alteration or modification of their rights. As part of the reorganization, the secured debts, the capital structure or the rights of stockholders must be changed and altered." (R.4-5)

Not only is it now abundantly clear that it is and will be impossible to formulate a plan for Legend City, Inc., in which the secured indebtedness can be paid off and the business remain in operation, it was so apparent at the time of the original filing that it was included in the debtor's petition for reorganization. Therefore, under the authority of *Arey & Russell, Leas,* and *Janaf, supra,* the petition showed on its face that it was not filed in good faith and should have been dismissed at the first instance. Since the secured creditors do not consent to an alteration of their rights, they must be paid off or given "a substitute of the most indubitable value." *In re Murel Holding Corp.,* 75 F.2d 941, 942 (2d Cir. 1955). This is clearly impossible.

Furthermore, beginning with the court's initial order of approval, it quickly became apparent that the debtor's petition was erroneous in part because the valuation alleged in the petition was completely out of proportion to the actual value of the assets. On January 19, 1965, eight days after the district court entered its initial order approving the petition of the debtor, and the same day that the appellants entered their appearance in the proceedings by filing the statement of attorneys pursuant to Section 210, 11 U.S.C. Sec. 610, the appellants, in a motion to dismiss the petition, stated that:

> "The mortgagees will not give their consent to any plan of reorganization which in any way modifies or alters their rights. Since, as is stated in the petition, any plan of reorganization must modify or alter their rights, there cannot be a successful plan of reorganization in this case and the petition must be dismissed since it was not filed in good faith."

Argument was held February 1, 1965 on the motion to dismiss. The burden of proof as to good faith in filing was on the petitioner-debtor corporation. *Marine Harbor Properties, Inc. v.*

Manufacturers Trust Co., 317 U.S. 78, 63 Sup. Ct. 93, 87 L. Ed. 64 (1942); *Grubbs v. Pettit,* 282 F.2d 557 (2d Cir. 1960); *In re St. Charles Hotel Co.,* 60 F. Supp. 322 (D.N.J. 1945), *aff'd,* 149 F.2d 645 (3d Cir. 1945), *cert. denied sub nom., Ladin v. Hurwith,* 326 U.S. 738, 66 Sup. Ct. 48, 90 L. Ed. 440 (1945). Nonetheless, petitioner-debtor did nothing more than rely on the book value of the assets which has been presented in its Section 128, 11 U.S.C. Sec. 528, petition. The district court required nothing more. Had the debtor corporation, in fact, been worth $2,000,000 more than the total of its liabilities, surely there would have been no need for a Chapter X proceedings. Nonetheless, the district court exercised its discretion and denied the motion to dismiss made by appellants.

In its pleadings, the debtor corporation had admitted that if, after a petition had been approved, it later became apparent to the district court that there was no reasonable prospect of effecting a plan of reorganization, it then became the court's duty to terminate the Chapter X proceedings (R.58). *John Hancock Mut. Life Ins. Co. v. Casey,* 141 F.2d 104 (1st Cir. 1944), *cert. denied,* 323 U.S. 713, 65 Sup. Ct. 39, 89 L. Ed. 574 (1944). Evidence of this kind was presented to the court at the time of the hearing of February 15, 1965, on the petition of the trustee for an order of the court authorizing him to issue his first certificate of indebtedness. It was abundantly clear at that time that the opposition of appellants to having their rights modified was sufficient under the cases cited earlier in this brief to negate any finding of a plan being feasible. It was clear at that time that it would be impossible to formulate or to get approval of a plan of reorganization in accordance with the provisions of Chapter X.

Even if the district court properly exercised its discretion in not dismissing the debtor's petition at that point, however, it thereafter became apparent that no plan of reorganization would be forthcoming, and that the trustee was merely using the reorganization provisions of the Bankruptcy Act to get a free ride at the expense of the secured creditors. One of the keystones of

Chapter X is the requirement that the trustee file a proposed plan for corporate reorganization. Indeed, it is toward that plan that the entire Chapter X proceedings are directed. It is a requirement of the Act that such a plan be presented within the soonest possible time, or, at the very least, that the trustee report to the court valid reasons why such plan cannot be formulated until a later date. Section 169, 11 U.S.C. Sec. 569. The court, in its initial order approving the petition, had set 60 days from the date of that order (which was later extended until April 1, 1965) as a reasonable time within which the trustee should prepare and file a plan or a report of his reasons why the plan could not be filed. The trustee then moved the court on March 22, 1965, for an order extending the time for proposing that plan to "the earliest date practicable."

This motion for an extension was filed immediately after the full hearing under Section 144, 11 U.S.C. Sec. 544, in which the court had just determined that the petition had been filed in good faith. In other words, evidence was presented to the court on March 5 and 19, 1965, that it was reasonable to expect that a plan of reorganization could be formulated and presented to the court in accordance with the provisions of Chapter X. Then, three days later, on March 22, 1965, the trustee came back to court stating that he could not prepare such a plan within the reasonable time ordered by the court. Even more significant, *such a proposed plan of reorganization has still not been presented, even though it is now well over a year later.* A year and a half from the date of filing of the original petition is not the "earliest practicable time," even under the terms of the court order extending time for filing a plan. After a year and a half, it becomes clear that the instant Chapter X proceedings are being used, and have been used from inception, as a mere "nursing receivership"—a use which has been condemned by the United States Supreme Court. *Continental Ill. Bank & Trust Co. v. Chicago, R.I. & Pac. Ry.,* 294 U.S. 648, 55 Sup. Ct. 595, 79 L. Ed. 1110 (1935). Similarly, the Seventh Circuit has stated:

> "If plans are not forthcoming with reasonable promptness, relief will be granted appellants. This bankruptcy proceeding contemplates a plan of reorganization. *This must be undertaken expeditiously aand proceeded with diligently. Such proceedings must never be viewed as nursing receiverships.* The two sections, 74 and 77, (11 U.S.C.A. § 202, 205) [Now included within Chapter X] are not to be used to delay, but to facilitate reorganizations of properties that are over-capitalized or whose capital structure is unfortunate. There is no basis for appellants to assume the court will not insist on the consummation of these ends." (Italics in the original.) *In Re Util. Power & Light Corp.,* 91 F.2d 598, 602 (7th Cir. 1937), *cert. denied,* 302 U.S. 742, 58 Sup. Ct. 144, 82 L. Ed. 573 (1937).

This authority was reaffirmed as to Chapter X proceedings in *In Re Burton Coal Co.,* 57 F. Supp. 361 (N.D. Ill. 1944) and *In Re McGann Mfg. Co.,* 190 F.2d 845 (3d Cir. 1951).

The passage of over a year and a half without trustee presentation of either a plan or of reasons why a plan cannot be effected, the continued deterioration of assets in which appellants have a security interest, the continued increase in liabilities, and, significantly, the vast increase in Chapter X administrative debt, the continued eroding of the position of the secured creditors, the continuing reaffirmation of the position of the secured creditors that they will not consent to any plan which would change their rights, the continued history of losses in operation, even under supposedly sound and experienced management and without the "sweetheart contracts," and the necessity of reinstating the "sweetheart contracts," if there is to be continued operation, all make it clear that the Chapter X proceedings which should not have been properly termed in good faith at their inception, have now degenerated into actual bad faith. The only part of the Bankruptcy Act which could possibly be applicable to this proceedings at this point is Section 236(2), 11 U.S.C. Sec. 636(2), which requires an order adjudicating the debtor a bankrupt or dismissing the proceeding. It is hard to conceive of a fact situation where feasibility of reorganization being effected is so lacking. The court

below will be fortunate, indeed, if there is sufficient estate for liquidation to repay the certificates of indebtedness which have been issued, let alone the administrative debt being incurred.

II. None of the Certificates of Indebtedness were Properly Issued in this Matter; Certainly No. 3 Was Not.

If we are right in the argument previously made, then, far from authorizing the certificate of indebtedness, the court should have put the debtor into bankruptcy. It not only did not do so but authorized a third certificate of indebtedness for $100,000, and that authorization is expressly challenged on this appeal. We incorporate by reference all that has been said going to the question of adjudication in bankruptcy; at a minimum, that same evidence and those same considerations forbid the third certificate.

There have been three separate orders of the district court authorizing trustee's certificates of indebtedness which may ultimately total $160,000 (R.100, 139, 640). This appeal is from the last of those orders, authorizing $100,000. Furthermore, there are unpaid real estate taxes, which by the orders of the district court, have priority ahead of Certificates of Indebtedness No. 1 (R.100). Under Arizona law those taxes are ahead of appellants' mortgage. *Ariz. Rev. Stat. Ann.* Sec. 42-312 (1956). Those taxes delinquent and due, currently amount to approximately $57,000 (T. III 286, 377). At this point, therefore, over $150,000 of claims could be placed ahead of the mortgage held by appellants, not counting the true administrative expenses which according to the trustee should amount to another $125,000 (T. III 378). In its April 15 order the court below specifically rejected the notion that the administrative debt should be subordinated to the new certificates.

Certificates Nos. 1 and 2, for $10,000 and $50,000 respectively, have been issued, the money has long since been spent, the certificates have not been repaid, nor is there any money available to the Trustee from which payment can be made. The order authorizing the issuance of Certificate of Indebtedness No. 3, for $100,000 is one of the orders appealed from here.

Unlike the preceding orders in which the sale of the certificate is made in a unit to a financial institution or an operator if it wishes to buy, the third certificate of indebtedness is in fact a plural certificate. By its terms it expressly contemplates a series of certificates which can be sold for as little as $10. It expressly contemplates that solicitation for this purpose shall be made among the existing stockholders and creditors of the debtor.[18]

Moreover, it is not settled what the priority of these certificates is to be. At the recommendation of the Securities and Exchange Commission, the question of whether these certificates shall be prior to the outstanding secured debt of the corporation or whether they shall take their place at the foot of the line is expressly reserved.[19]

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[18]The relevant passages of the order are:

"ORDERED that Certificate of Indebtedness No. 3 may be issued serially in amounts not to exceed the total sum of One Hundred Thousand Dollars ($100,000.00) provided, however, that no single certificate shall be issued as a part thereof in an amount less than Ten Dollars ($10.00); and it is further . . .

ORDERED that in the sale of said certificates, solicitation shall be limited to stockholders, unsecured creditors and secured creditors; provided, that any other persons may purchase said certificates without solicitation. . . ." (R.640, 643-44)

[19]The Court's order provides:

"ORDERED that if there be no such income or if such income is insufficient to repay said Certificate of Indebtedness No. 3, then said certificate of indebtedness shall be paid as a cost and expense of administration and a liability of the Trustee out of the unencumbered or free assets of LEGEND CITY, INC., provided, however, that the above-entitled Court reserves jurisdiction to determine upon proper notice and hearing to what extent, if any, said certificate of indebtedness shall be accorded a lien status prior to the mortgage or lien of secured creditors of LEGEND CITY, INC." (R.641).

The SEC had filed a memorandum advising the Court that:

". . . . the Court should reserve jurisdiction to determine at a later date the extent to which, if at all, the trustee's certificates should be given any priority over the secured creditors of the debtor corporation. There is no need to resolve this issue at this time. In a proper case, it has been held that the Court would be justified, should reorganization fail, in charging certain expenses of the aborted proceeding against secured assets,

(Continued on Page 30)

The order, in short, creates a sort of financial double jeopardy for everyone involved. The original investors, having lost their shirts, are now given the opportunity under the imprimatur of a federal district court to divest themselves of another garment as well; while if the poor original creditors, whose only offense is that they advanced several hundred thousands of dollars on the note and mortgage, should now wish to try to sell that obligation, neither they nor their purchaser would know whether this third certificate comes before or after their securities.

When the court under Sec. 116(2), 11 U.S.C. 516(2), authorizes certificates of indebtedness, it exercises a broad grant of power which must be exercised cautiously. The court may only "upon cause shown" authorize a trustee to issue Certificates of Indebtedness, ". . . upon such terms and conditions and with such security and priority in payment over existing obligations, secured or unsecured, as in the particular case may be equitable."

As stated in the leading case:

> "The exercise of the power to authorize the issuance of trustee's certificates and to supplant the existing first mortgage calls for careful, cautious and considerate action by the

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when the free or unencumbered assets are insufficient. *First Western Savings & Loan Ass'n* v. *Anderson,* 252 F.2d 544 (C.A. 9, 1958); *In re Alaska Plywood Corp.,* 166 F. Supp. 423 (D.C. Alaska, 1958). The rights of the certificate holders as a cost and expense of administration vis-a-vis the secured creditors under the above-cited authority should be determined along with other costs and expenses of administration if and when the issue should arise.

Accordingly, the Commission makes no objection to the proposed financing. The suggested priority status is, we believe, 'equitable' under the circumstances as provided in Section 116(2) of Chapter X." (R.634).

It is no great wonder that the SEC makes no objection to the proposed financing. Neither the SEC nor the stockholders are underwriting it. If the new certificates are given priority over the appellants' security, however, the appellants will be underwriting the financing and sustaining the losses which are surely to come from the operation of the park. This matter is discussed at Section III of this brief.

> court. Such power should not be abused by an unwise exercise of discretion. . . . If the Court does not so approach the question, but acts merely on hopes unsupported by facts, its order 'in the particular case' will not be 'lawful' [the statute now reads 'equitable' instead of 'lawful']. On appeal it will be reversed." *In Re Prima Co.,* 88 F.2d 785, 790 (7th Cir. 1937).

The *Prima Co.* case involved a corporation which had much perishable property which would have been lost if liquidation occurred. The reorganization court had authorized Trustee's Certificates of Indebtedness equalling less than three quarters of one per cent of the value of the debtor's property. The known losses on liquidation would have been three times the value of the certificates issued. The court found the authorization of the issuance of the certificates to be valid.

How different that fact stiuation was! The Court below is not dealing with the problem of authorizing trustee's certificates for a certain amount of money in order to preserve property worth far more money and which otherwise would be lost, but after the trustee's certificates are issued surely will be saved. Here, the total amount of trustee's certificates amount to from 10 to 30 per cent of the value of the estate, depending on the appraisal. Issuance of the third certificates surely is an act "merely on hopes unsupported by facts." As the Supreme Court of Washington once said, referring to mining operations near a ghost town,

> "Like the town of Bolster they have no present but live in the memories of the past and in hope for the future, and the future is based upon visions too remote for the law to recognize." *Thorp v. McBride,* 75 Wash. 466, 135 Pac. 228, 229 (1913).

Like the town of Bolster, any hopes of the trustee and the stockholders for the future of Legend City are based upon visions too remote for the Bankruptcy Act to recognize.

The statute, Section 116(2), 11 U.S.C. Sec. 516(2), requires the trustee to show cause for the issuance of certificates. However,

at the time that Certificate of Indebtedness No. 1 for $10,000 was authorized, before the Trustee first reopened the amusement park, there was not sufficient cause shown to warrant the issuance of a Trustee's certificate that would in any way impair appellants' security. With regard to Trustee's Certificate of Indebtedness No. 3, appellants have not only rebutted the trustee's attempted showing of cause for its issuance, but have also affirmatively proved that no Trustee's Certificates of Indebtedness should be issued of any kind or priority.

At the time Certificate of Indebtedness No. 1 was authorized, the situation in which the debtor corporation found itself was much like the situation of the parties in *In re Prima Co.*:

> "In brief, it must be apparent that where a debtor in financial straits, hard pressed to keep its head above water, goes into a court of bankruptcy to reorganize, it is natural and quite likely that the creditors will be aligned into two sharply divided camps. One group represents the unsecured creditors and the stockholders. They have nothing to lose by a continuation of the business. Opposed to this group is a second, composed of the secured creditors who insist upon the immediate realization of their claims. The first class visions nothing but a rosy future with all debts ultimately paid and the stockholders in full possession of their property, with management unvexed by creditors' supervision and unembarrassed by unsolicited creditor advice, enjoying substantial dividends which are the just reward of keen foresight and great courage. The secured creditor, on the other hand, is apt to fear much and to have gloomy forebodings of a dismal future, darkened by shadows of the unforeseen. The plan this group advocates may be and often is selfish, but the secured creditor can consistently and stoutly assert that he did not invest his money as a speculation, as did the stockholders and some of the unsecured creditors. If he overstresses his rights, belittles the existence and value of the equities, and if his position seems somewhat unfair, as well as unsympathetic, in view of the total assets compared to the small amount of the mortgage indebtedness, the court should nevertheless never take any serious chance of impairing his

> security to merely postpone the evil day to unsecured creditors and stockholders. If the court does not so approach the question, but acts merely on hopes unsupported by facts, its order 'in the particular case' will not be 'lawful.' On appeal, it will be reversed." *In Re Prima Co.,* 88 F.2d at 790.

Assuming for the sake of argument that the district court was originally acting within its discretion to allow the stockholders and unsecured creditors to attempt to realize the rosy future which they envisioned, it is now clear that the gloomy predictions of the secured creditors were far more accurate appraisals of the park's future.

The secured creditors claimed their security was in danger in the first pleading they filed (R.27) and have continued to do so ever since. They were met, however, by the trustee's assertions that all that was necessary to run the park at a profit and provide money for everyone was:

1. An experienced park operator of his choice to operate the park.
2. Installation of sound management practices and procedures.
3. Adjustments on percentages to be received from concessionaires.

The district court authorized the trustee to obtain, and he did obtain:

1. An experienced park operator of his choice to operate the park.
2. Installation of sound management practices and procedures.
3. Adjustments on percentages to be received from concessionaires.

Even so, the trustee's estimates of profit to be made by operating the park were in error by a quarter of a million dollars (T. III, 170-171), and the park's deficit grew $206,000 in one calendar

year (T. III, Exhibit 8). It has continued to grow since December 31, 1965.

Even if the district court were justified in 1965 in taking the serious chance of impairing the security interest of the secured creditors (and a very serious chance indeed was taken, as is evidenced by the financial analysis of the corporation earlier in this brief) the court cannot do so again. The only really competent evidence of value of the debtor's property is the professional M.A.I. appraisal showing the land valued at $450,000 (T. I 79) and the Trustee's estimate that on liquidation, the personal property is worth no more than $250,000 to $300,000. (T. III 383). This is the estimate of value closest to true value. The estimate of "going concern value" in the record is baseless in fact and is not an estimate by a qualified expert. See the statement of facts, footnote 14, for the exact basis on which that estimate was given. Considering the history of operating losses of this business, there can be no going concern value — it is not a going concern. The security is therefore not worth as much as the overall indebtedness to appellants which is secured by that property. By issuing Certificates of Indebtedness Nos. 1 and 2 the court was taking a serious chance of impairing appellants' security. By authorizing the issuance of Certificate of Indebtedness No. 3 the court is unquestionably destroying the security of the appellants. This the court cannot do.

The entire philosophy of Chapter X is that the secured creditors are to realize the full amount of their liens before anyone else can realize anything from either the reorganization or the liquidation. This is aptly called the rule of absolute priority. Senior claimants are entitled to full compensatory treatment for the rights they possess before anything may be allocated to any junior interests. They must get the "indubitable equivalent" of their security. This principle was first developed in railway reorganizations, *Northern Pac. Ry. v. Boyd,* 228 U.S. 482, 33 Sup. Ct. 554, 57 L. Ed. 931 (1913), but is fully applicable to this type of proceeding. *Consolidated Rock Prod. Co. v. DuBois,* 312 U.S. 510, 61 Sup. Ct.

675, 85 L. Ed. 982 (1941). Since in successful reorganizations, where a plan is finally entered into and carried out, the plan must provide for payment of secured creditors or for an indubitable equivalent to payment, it is all the more clear that the secured creditors must get the security they received when the reorganization fails and that is all with which they are left.

There are further requirements for the issuance of Trustee's Certificates of Indebtedness which also have not been met with respect to any of the certificates authorized by the district court and particularly the new class authorized. There must be a high degree of likelihood that the debtor can be reorganized by a feasible as well as a fair and equitable plan in accordance with the act within a reasonable time, and there must be a high degree of likelihood that the secured creditors will not have their security injured by this procedure. *In Re Third Ave. Transit Corp.,* 198 F.2d 703 (2d Cir. 1952). It is inconceivable that the court could have found as a fact, based upon the entire record before it and the hearings held in March, 1966, a "high degree of likelihood" either that the debtor could be successfully reorganized quickly or that the secured creditors would not have their security injured by this procedure. The 1965 operating history of the trustee could only lead to the opposite conclusion that reorganization of the debtor is impossible.

The *Third Ave. Transit Corp.* case did not directly concern Trustee's Certificates. It involved a Trustee's request for possession of property in the hands of the mortgagee. The two proceedings are analogous, however, and their effect is the same when there is not or may be not sufficient property to satisfy the debtor's secured debts.

> "The first mortgage bond holders should not have had their security put at risk in order to increase the 'elusive equity' of the junior creditors or stockholders, for those junior interests possess no right to a 'run for other people's money.' To direct enforced lending of the sort ordered here may yield these undesirable results: (a) The zeal of the reorganization

> trustees to make only the most prudent expenditures may be blunted. (b) There may well be undue delay of what may be inevitable liquidation. (c) The judge loses the opportunity to learn, in a significant way, the detached attitude of the commercial world toward the value of the assets." *In Re Third Ave. Transit Corp.,* 198 F.2d at 707.

The *Third Ave. Transit Corp.* case also imposes a requirement that the Trustee show that the secured creditors will not be injured by the issuance of the Trustee's Certificates of Indebtedness. This, as has been elaborated elsewhere, the Trustee has not shown.

The third possible undesirable result stated in the *Third Ave. Transit* case is significant here. The reaction of the commercial world to the possible marketing of evidences of indebtedness can be of great help to the court in analyzing the financial position in which the debtor finds itself. As the court stated in the *Third Ave. Transit* case:

> "Indeed, if, in the ordinary market, funds can be procured only on severe terms, that fact will often throw light on the likelihood of reorganization. . . ." 198 F.2d at 706, footnote 9.

The detached attitude of the commercial world is most significant in the case of Legend City, and, in fact, considerable testimony was given about that attitude at the hearing in March, 1966. The trustee testified that he, as was the case with the debtor's management which preceded him, was rebuffed by every sophisticated lender that he approached for financing. (T. III 394). He talked to eastern banks, the Small Business Administration and several western banks. (T. III 394-395). Instead, it was necessary for the trustee, in order to raise any money, to borrow it in small amounts from the stockholders and unsecured creditors, whom even the trustee terms unsophisticated lenders. Not being able to convince any normal lender, the trustee turned to the people least able to protect themselves. The Securities and Exchange Commission, which has appeared in these proceedings supposedly to protect the public investors, indicated throughout the hearing that it would require full disclosure to the would-be

purchasers of Certificate of Indebtedness No. 3 and along that line, required a number of changes in the proposed disclosure of the trustee. Appellants find the notion that so-called disclosure is really going to protect these unsophisticated lenders nothing more than fantasy. The SEC is a participant in these proceedings because of Sections 161, 11 U.S.C. Sec. 561, and 208, 11 U.S.C. Sec. 608. The position of the Commission is supposed to be to protect the stockholders, and the only way to protect those stockholders who have been foolish enough to buy the trustee's certificates is to attempt to give them priority over appellants' mortgage. Sympathy notwithstanding, this is a possibility that appellants cannot allow and that no court should permit.

Throughout these proceedings, much has been made of the fact that the debtor corporation has many small shareholders whose investments should be preserved if at all possible. In this respect, counsel for the debtor and the trustee and the shareholders committee seem to equate this private corporation, founded to make a profit and subject to known market risks, with a quasi-public utility status. This has no bearing on appellants' legal rights to repayment or, in the alternative, to their contracted-for security. But even if this somehow does have relevance, it is not conclusive of the issue. A true public utility was the debtor in *In re Third Ave. Transit Corp., supra,* yet the Second Circuit stated:

> "As the debtor is a public utility, the judge properly took into account the factor of the public interest in the debtor's continued operations. That, however, is but one factor; it must not be allowed to outweigh all others. There are strict limits to the extent to which, in reorganization proceedings, the interests of creditors (or of a particular class of creditors) may be sacrificed to the public interest; to exceed those limits is (to say the least) to come dangerously close to the edge of unconstitutional taking of property, a line from which courts should keep away if possible." *In re Third Ave. Transit Corp.,* 198 F.2d at 707.

This Court should reverse the court below and direct the return

of any impounded funds remaining from the sale of the new certificates to the certificate purchasers pro rata.

III. The Court Cannot at Some Later Time Determine the Priority of Certificate No. 3.

Whether or not it was reversible error for the district court to authorize the issuance of Certificate of Indebtedness No. 3, it is nonetheless a fact that as of May 18, 1966, at least $35,000 of these certificates have been sold by the Trustee to unsophisticated (and undoubtedly unsuspecting) public stockholders of the debtor. As a practical matter, therefore, some arrangement must be made for the method of their repayment if, at the time of repayment, there are sufficient assets to do so. The district court, however, has not done this. It has reserved jurisdiction or attempted to do so in the April 14, 1966 order here appealed from, ". . . to determine upon proper notice and hearing to what extent, if any, said Certificate of Indebtedness shall be accorded a lien status prior to the mortgage or lien of secured creditors of Legend City, Inc." This device of approach is totally lacking in authority or support. *First Western Sav. & Loan Ass'n v. Anderson,* 252 F.2d 544 (9th Cir. 1958), cited by the SEC to the court below (see footnote 19, *supra*) will not tolerate such an interpretation. The unsophisticated purchasers deserve better treatment if in fact disclosure means anything. In addition, the appellants have a right to know more.

Elsewhere in this brief, it is established that the issuance of these certificates of indebtedness was error and also that it is error for the court to allow the trustee to continue operating the debtor's business. The fundamental reason for this is that the security of the appellants is being endangered by these courses of action. These same principles, therefore, show that the new Certificates of Indebtedness, when issued, should not further impair the security of the secured creditors and that it is an abuse of whatever discretion the district court may have had to allow them to do so. Since it is an abuse of discretion for the court to issue these certificates because their existence may impair appellants' security, the court cannot allow those Certificates which

were erroneously issued to directly impair the security. Even if this Court should find that the certificates were not improperly issued, nonetheless it is still the law that they cannot directly impair appellants' security at this time, and therefore must be placed in priority and right in liquidation or reorganization after the note and mortgage of appellants.

The net effect of the court's reserving or attempting to reserve jurisdiction to set the priority of these certificates is twofold. It places the mortgagees (the appellants) in the position of not knowing exactly what it is that they own. For example, if appellants were to secure a buyer for their mortgage interest (and their mortgagees' interest in the property is certainly a marketable item, even though the market is not good) they could not accurately inform a prospective buyer what it is they have to sell. The value of appellants' security would be greatly altered if there was another $100,000 ahead of them in priority, particularly since the value of the real and personal property securing the note is apparently not sufficient to pay off the property taxes and the Certificate of Indebtedness now purportedly ahead of appellants and to pay off appellants as well. The Court's ruling, therefore, makes property and rights of the appellants, which certainly should have some present value, worthless. They will have value only when the priority of the new certificates is ultimately determined and an accurate assessment can be made of value.

The fact that the district court has reserved jurisdiction to set the priority of these certificates in and of itself shows under these circumstances that its order of April 14, 1966 was erroneous. There is only one situation in which the priority position of Certificate of Indebtedness No. 3 would be significant — that is, the situation in which the value of the debtor's property is insufficient to pay off those obligations now ahead of the secured creditors, the secured creditors and the Certificate of Indebtedness No. 3. The fact that the court reserved jurisdiction to set the priority, or attempted to do so, in and of itself shows that the reorganization court is concerned that perhaps the debtor's prop-

erty may not be worth enough to pay off these three classes. The court has tacitly said it concurs with what appellants have been saying all along. If the court is concerned about this fact, the rule of absolute priority as well as the principles set forth in the other cases cited in this brief clearly show that the certificates should not have been issued in the first place and that, if issued, they *must* be put in a priority position after and junior to the appellants' mortgage. If there is not enough debtor property to insure the payment of all three classes, placing Certificate of Indebtedness No. 3 ahead of the appellants' mortgage would be directly contrary to the rule of *Northern Pac. Ry. v. Boyd, supra,* and to the principles and philosophy of Chapter X.

This situation is further aggravated by the fact that the $100,000 to be raised in this manner is to be used for working capital for the trustee's 1966 operation. The professional operator the trustee had thought imperative is long gone. The trustee once admitted he is not qualified to run the amusement park, and yet that is exactly what is happening in the summer of 1966. The trustee's contract with the former operator, T. H. Browning & Associates, expressly provides that "the operation of a park is a specialized business requiring the assistance by the trustee of experienced operators of this type of business . . ." (R.148).

The court below did not and could not suppose that the trustee, Mr. Fulford, was an expert in operating an amusement park. Not only did he so acknowledge at T. III 164, but after an exchange on this point, the court observed:

> "The Court: He may be an expert trustee.
>
> "Mr. McGarry: I would concede that Mr. Fulford is an expert trustee, but he is no expert in the amusement park business, Your Honor, as he just conceded.
>
> "The Court: Well, I think we all understand that." (T. III, 164).

The trustee is not an expert on the condition and safety of amusement park rides. He is not an expert on the consequences of labor disputes to amusement park attendence although he

lames much of the decrease in attendance at Legend City during 965 on this cause (T. III 165-66). His general and complete ack of knowledge in this field is fully substantiated by the fact hat his projected estimate of the net profits for his 1965 operaions was in fact a quarter of a million dollars in error (T. III 70-171).[20]

Despite this demonstrable lack of experience in a very technical nd complex business, the trustee proposed to use funds obtained y the sale of Certificates of Indebtedness No. 3 to unsophisticated urchasers to reopen the park and operate it again (T. III 359). he risk of his continuing the to date invariable course of failure an only be put upon the secured creditors and this is precisely he result if Certificates of Indebtedness No. 3 is given priority ver them. The use of funds for working capital by inexperienced dministrators leaves secured creditors with nothing of substantial alue in return and this is precisly what courts must prevent. *n re Third Avenue Transit Corp., supra.* Certificate No. 2 for $50,000 is a clear case in point; this amount was placed ahead f the common creditors and there is now nothing at all to show or it. Stockholders and creditors cannot be compelled to use their noney to provide temporary pleasure for the patrons of the egend City Amusement Park.

V. The Motion for Sequestration of Rents and Profits Under These Circumstances Should Have Been Granted.

At the same time the district court authorized the issuance by he trustee of Certificates of Indebtedness No. 3, it also denied ppellants' motion to sequester the rents and profits, if any, of he operation during the 1966 season. As mentioned earlier, the nortgage of appellants covers not only the real property owned y the debtor corporation and the personal property thereon, ut it also covers the debtor corporation's interest in leases, licenses nd franchises, and it specifically covers "all rents, issues, profits

[20]In assessing the effect of his 1965 operating season, the trustee failed r refused even to examine figures from operation of the previous years (T. III 356-57).

and other money, now due or which may hereafter become due to the mortgagor from the ownership, lease, use, occupancy, or other exploitation of any other nature whatsoever of all or any portion of the premises described in Exhibit A." (T. III Exhibit I) Exhibit A to the mortgage is the legal description of the Legend City amusement park located on West Washington Avenue, Tempe, Arizona. The mortgage has been in default for a substantial length of time, at least since October 28, 1964, and is currently being foreclosed in state court proceedings subject to the continued supervision of the district court. Already much of the security for the mortgage has been destroyed by the acts of the trustee in the trustee's attempt to, without judicial sanction, break the leases and leasehold interests of the debtor in the concession agreements.

Appellants specifically petitioned this court for an order of sequestration of the rents and profits of the operation of the business since the appellants had a security interest therein. This was a proper motion and the court has the power to grant it. 4 *Collier, Bankruptcy,* ¶70.16 (14th ed. 1964); *Investors Syndicate v. Smith,* 105 F.2d 611 (9th Cir. 1939). The court would have been able to impound the monies received in 1966 over and above the 1966 operating costs so that if the secured creditors' claim was for some reason not fully paid, the impounded fund would be available. This was clearly contemplated by the mortgage.

The motion should have been granted in this case. Rents and profits should not be sequestered if the sequestration would put the mortgagor in a better position than he would have had, had bankruptcy not intervened. Otherwise, it should be granted. *Investors Syndicate v. Smith, supra.* Here, if the bankruptcy had not intervened, the appellants, as a matter of state law, could have had the rents and profits derived from any operation of the amusement park applied to interest and principal on their mortgage. The receiver appointed by the state court was originally forbidden for the time being from operating the property. None-

heless, he might have been authorized to lease the park and had he park in fact been reopened during the pendency of state court roceedings, the appellants would have had the rights to rents and rofits after operating costs and taxes were paid in accordance vith their assignment. No different result is or was sought here.

It must be emphasized that the appellants did not and do not eek to have every nickel and dime taken in for the payment of dmission to every ride in the amusement park applied to the nortgage debt. Rather, the motion is directed to the rents and rofits — that portion of the 1966 cash flow which is left over fter the true operating expenses or trade payables are paid from he operating income. If the 1966 season resembles the 1965 eason, the motion will be moot, since there was no operating rofit. Indeed, all indications are that this will be the case. Nonetheless, it was error for the court to deny the motion on the ventuality that there might be an operating profit.

The secured position of appellants is in additional jeopardy ecause of the denial of the motion since the security for which he appellants bargained will be further diminished and the ppellants may be required to pay costs and expenses which hould fall upon the general unsecured creditors who did not ely on any security when they extended credit to the debtor orporation. *Mortgage Loan Co. v. Livingston,* 45 F.2d 28 (8th Cir. 1930). This Court should direct impoundment of any 1966 verflow funds to fully secure appellants.

CONCLUSION

It has been over eighteen months since the debtor's petition for reorganization under Chapter X was filed. During those eighteen months, the trustee has asked for and received authority to do as much, if not more, with the debtor's property than any trustee in the history of Chapter X. The appellants have objected to almost every act which the trustee has done, although the appellants did agree finally to give the trustee a chance to operate the park during the 1965 season to see if a profit could be made. Time has proven that the objections were well taken. The result is now clear. A profit cannot be made. The trustee, however, intends to keep going as long as the district court will let him. Meanwhile, the appellants have not received protection of any kind. Even those rulings which the district court made which could be construed to provide some protection to the secured creditors by requiring preservation of the property have been totally ignored by the trustee. The court's initial order of approval directed the payment of property taxes, and Certificate of Indebtedness No. 1 was specifically worded in such a manner as to require payment of property taxes, yet the trustee has totally disregarded that order.

In April, 1964 appellants bargained for and received security for the funds which they loaned. They did not bargain for an obligation to finance the continued operations of an amusement park with no compensation or debt service for a period of several years without any opportunity to formulate a plan for or to participate in the management of the park. Yet that also they received.

The debtor corporation has had its chance. The Chapter X Trustee has had his chance. The stockholders have had their chance. The Securities and Exchange Commission has had its say. Now it is time for the creditors to receive that which they should have received eighteen months ago. The orders of the district court appealed from should be reversed and the case remanded with instructions to the district court to forthwith adjudicate the

ebtor corporation a baankrupt. The liquidation trustee should be irected to apply all monies received from the Chapter X Trustee o the payment of the unpaid property taxes and impound the alance, if any, to apply on appellants' secured debt to the extent ecessary to satisfy it in full.

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Phoenix, Arizona
Attorneys for Appellants

uly, 1966

I certify that in connection with the preparation of this brief, have examined Rules 18 and 19 of the United States Court of Appeals for the Ninth Circuit, and that, in my opinion, the foregoing brief is in full compliance with those rules.

JOHN P. FRANK

(Appendix Follows)

APPENDIX A

EXHIBITS

Exhibit No.	Identification	Page No. of T. III where identified	Page No. of T. III where admitted
1	Document - "Monthly 1965 Season Attendance - Receipts and Per Capita Patron Expenditure.	11	12
2	Document - "Necessary Employees - Three Days a week - Cost per Month"	11	19
3	Document - "Projected Fixed Costs of Operation Per Month Operating on a Three-Day Week for the Months of May, June, July, August and September, 1966."	19	21
3A	Document - "Projected Fixed Costs of Operation Per Month Operating on a Three-Day Week for the Months of May, June, July, August and September, 1966."	45	45
4	Projected Income Per Month for the Months of May, June, July, Aug. and Sept., 1966, Based on May, 1965 Attendance.	20	22
5	Fulford-Browning Balance Sheet, Dec. 31, 1965	26	28
6	"Statement of Costs for Securing Legend City for January 1966."	26	28
7	"Statement of Daily Operation of Legend City, May 1, 1965 through Nov. 30, 1965."	29	29
8	Balance Sheet December 31, 1965.	76	133
9	Projected Income Analysis for the Operating Season of 1966, May through September.	114	116
10	Fulford-Browning statement of income and expense for the period May 1 to November 30, 1965.	116	116
11	Report of the Trustee, July 31, 1965.	140	140

APPENDIX B

Walter E. Fulford, Trustee and Browning & Associates
STATEMENT OF INCOME AND EXPENSE
For the Period May 1, 1965 to December 31, 1965

Revenue		$656,794.22	
Less: Adjustments to Revenue		4,151.29	$652,642.93
Cost of Sales		$ 71,761.90	
Concessionaire Expense		101,737.81	173,499.71
GROSS PROFIT			$479,143.22
Payroll		$209,096.28	
Payroll Taxes		13,727.05	
Power		20,922.74	
Water		4,999.50	
Gasoline, Oil & Lubricants		5,603.84	
Music & Entertainment		16,994.79	
Advertising & Publicity		38,306.93	
Promotion		7,629.21	
Laundry & Uniforms		1,101.76	
Depreciation		19,523.21	
Travel		507.29	
Entertainment		333.28	
Administrative Expenses			
Travel	5,363.66		
Entertainment	2,939.59		
Subsistence	7,840.78	16,144.03	

ffice Supplies & Expense	1,479.84	
elephone & Telegraph	6,067.00	
ofessional Services	2,197.05	
ostage	543.60	
inting	5,522.22	
operty Taxes	10,945.52	
censes, Fees & Taxes	1,041.35	
les Tax	16,969.87	
nortization of Fit-Out-Costs	21,908.88	
terest Expense	3,332.34	
sh Over & Short	354.28	
ental Expense	5,549.25	
pplies	21,036.11	
epairs & Maintenance	14,813.32	
surance	29,819.56	
otection Service	21,647.12	
eight	732.07	
ntributions	238.21	
iscellaneous Expense	4,244.99	
ad Debt Expense	208.65	523,541.14
ET LOSS: Walter E. Fulford & Browning & Associates		(44,397.92)

APPENDIX C

WALTER E. FULFORD
Trustee for
LEGEND CITY, INC., AN ARIZONA CORPORATION
TEMPE, ARIZONA

RECONCILIATION OF NET LOSS
For the Twelve Months Ended December 31, 1965

Net Loss - Walter E. Fulford, Trustee and Browning & Associates		$ 44,397.92
Expenses - Walter E. Fulford, Trustee Debtor Corporation		
Wages and Payroll Taxes	$ 3,247.51	
Power	801.11	
Office Supplies and Expenses	32.44	
Telephone and Telegraph	86.04	
Professional Services	1,233.90	

Interest Expense	736.60		
Rental Expense	77.68		
Repair and Maintenance	19.74		
Insurance	3,837.00	$ 10,072.02	
Expenses - Walter E. Fulford, Trustee For Legend City, Inc., An Arizona Corporation:			
Depreciation	$ 98,100.00		
Interest	48,295.20		
Property Taxes (1-1-65 to 5-1-65)	5,472.76	151,867.96	161,939.98
NET LOSS			$206,337.90

APPENDIX D

Legend City, Inc.,
BALANCE SHEET
December 31st, 1964

ASSETS

Current Assets:			
Cash on Hand and in Banks	$ 1,123.74		
Accounts Receivable	8,212.04		
Notes Receivable	90.00		
Inventories—Supplies	16,212.19		
Prepaid Expenses	12,076.38		
Total Current Assets		$	37,714.35
Park Land, Buildings and Equipment:			
Land and Land Improvements	$1,151,851.27		
Buildings and Equipment	2,767,523.13		
	3,919,374.40		
Less—Reserve for Depreciation	193,078.08		3,726,296.3
Other Assets:			
Organizational Expense	$ 1,337.94		
Trade Mark	245.00		
Refundable Deposits	14,005.00		15,587.9
Total Assets			$3,779,598.6

LIABILITIES AND CAPITAL

urrent Liabilities:			
Accounts Payable	$ 165,657.60		
Notes and Contracts Payable	130,509.77		
Accrued and Withheld Payroll Taxes and Insurance	25,341.43		
Other Accrued Expenses and Taxes	55,780.57		
Total Current Liabilities		$ 377,289.37	
ong-Term Liability			
Mortgage Payable		636,486.29	
eferred Credits			
Advance Rentals		14,422.20	
apital Stock:			
Class A Common Voting Stock	$ 926,591.00		
Class B Common Voting Stock	97,911.00		
Premium Received on Class A Stock	2,268,267.00		
Earned Surplus (Deficit):	($402,572.99)		
Add—Net Loss for Eleven Months Ending December 31st, 1964	(138,795.33)		
Earned Surplus (Deficit), December 31st, 1964		(541,368.32)	2,751,400.75
Total Liabilities and Capital			$3,779,598.61

APPENDIX E

WALTER E. FULFORD

TRUSTEE FOR

Lengend City, Inc., an Arizona Corporation

Tempe, Arizona

December 31, 1965

BALANCE SHEET

December 31, 1965

ASSETS

Current Assets:			
Cash on Hand and in Banks	$ 3,668.05		
Accounts Receivable	8,674.07		
Notes Receivable	90.00		
Inventories	19,198.22		
Prepaid Expenses	34,729.00		
Total Current Assets		$	66,359.3
Park Land, Buildings and Equipment:			
Land and Land Improvements	$1,151,851.27		
Buildings & Equipment	2,841,087.01		
	$3,992,938.28		
Less: Reserves for Depreciation	310,701.29		3,682,236.9
Other Assets:			
Organizational Expenses	$ 1,337.94		
Trade Mark	245.00		
Refundable Deposits	24,824.00		
Equity in Equipment Contracts	14,629.54		41,036.4
TOTAL ASSETS			$3,789,632.8

LIABILITIES AND CAPITAL

rrent Liabilities:			
Accounts Payable (Prior to 1-8-65)		$ 165,657.60	
Accounts Payable (Subsequent to 1-8-65)		37,438.72	
Insurance Premiums Payable		5,677.27	
Accrued and Withheld Payroll Taxes and Insurance		36,397.74	
Notes & Contracts Payable (Current Portion)		177,142.00	
Accrued Interest Payable		63,621.24	
Accrued Property Taxes Payable		32,661.30	
Other Accrued Taxes and Expenses		21,365.60	
Mortgages Payable		138,638.94	
Total Current Liabilities			$ 678,600.41
ong-Term Liabilities:			
Notes and Contracts Payable	$230,842.00		
Less—Due within one Year (above)	177,142.00	$ 53,700.00	
Mortgage Payable	$ 636,486.29		
Less—Due within one year (above)	138,638.94	497,847.35	$551,547.35
eferred Credit:			
Advance Rentals			14,422.20
apital:			
Class A Common Voting Stock		$ 926,591.00	
Class B Common Voting Stock		97,911.00	

Premium Received on Class A Stock		2,268,267.07	
Earned Surplus (Deficit) January 8, 1965	$(541,368.32)		
Add—Net Loss for The Twelve months ended December 31,1965	(206,337.90)		
Earned Surplus (Deficit) December 31, 1965		(747,706.22)	2,545,062.85
TOTAL LIABILITIES AND CAPITAL			$3,789,632.81